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Pacific struggles

Agrium's strategy goes awry as Alaska plant closing looms, Australian project off

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Several years ago, Agrium Inc. appeared to be making giant strides in a plan to capture a healthy share of the lucrative Pacific market for nitrogen fertilizer. Today, the company is struggling to play a part in the Pacific trade at all.

Agrium's Pacific approach hinged on two strategically located plants, one on Alaska's Kenai Peninsula, to serve the North Pacific, and in the south, a now-abandoned proposal for an Australian plant positioned well to ship to South Asian markets.

Agrium is the biggest nitrogen fertilizer maker in the Americas but it wants more of the Pacific fertilizer market, despite the setbacks it has endured in the region.

"The Pacific Rim is a growth area, with a rising standard of living," Christine Gillespie, Agrium investor relations manager, told Petroleum News in early 2004. "People are

Agrium extends deadline

Cook Inlet gas producers now have until May 13 to respond to a request by Agrium for additional gas to feed its Kenai nitrogen plant. Agrium extended the deadline because some of the producers asked for additional time to respond, Agrium spokeswoman Lisa Parker told Petroleum News April 18. The initial deadline was April 15.

In its March request, the company offered \$3 per thousand cubic feet of gas to Cook Inlet producers, a significant jump over the historic \$2 per mcf average gas price paid for delivered supply to its Kenai plant. High recent prices for nitrogen fertilizer on the world market made the higher offer possible.

Failing a new gas supply, the plant will close when its current supply contract expires on Oct. 31.

wanting higher food quality, and it takes more fertilizer to make beef than rice.”

Gillespie said population growth in Asia is driving the market for fertilizer upward as farmers strive to produce more food from a finite supply of farmland.

Worldwide, the market for nitrogen is competitive, and production is increasing. To prosper, producers need an advantage in one or more of three key areas — natural gas feedstock price, facility cost or proximity to market.

Alaska plant to close

Agrium’s Kenai, Alaska, plant has a major problem its geographic advantages can’t overcome. The company says it can’t get enough competitively priced natural gas from Cook Inlet fields to continue operating the plant. Natural gas is the highest cost component in the production of the plant’s primary product — anhydrous ammonia — accounting for 80 percent to 90 percent of the manufacturing cost. The plant is scheduled to close in November, when its current supply contract expires.

Alaska-produced nitrogen enjoys a proximity-to-market advantage in Korea. Agrium also sells Kenai-produced anhydrous ammonia and urea to Mexico, with smaller deliveries to Thailand, the United States, Australia and New Zealand. All of the plant’s output is carried by ship, except for a small amount used in Alaska for fertilizer.

Korea’s fertilizer consumption growth may be held in check to some degree by recent government policies designed to eliminate massive rice surpluses, but its economy relies on imports of ammonia and urea. Alaska — due to its proximity and political stability — is a preferred trade partner in the Korean market. It is likely Agrium’s Kenai plant will continue to hold a strong market share in Korea, if the

company can find the gas it needs to keep the plant open.

Australia abandoned

After a three-year fight to keep its Australian nitrogen plant proposal alive, Agrium walked away from the Australian end of its Pacific plan. Wholly owned subsidiary Agrium Australia Pty Ltd. recently abandoned plans to build a nitrogen plant on Western Australia's Burrup Peninsula. The plant was proposed near major natural gas deposits on the North West Shelf. The plant's proximity to Asian markets gave the location an edge over Middle East suppliers, offsetting higher natural gas prices in Australia.

West Perth, Australia-based Chemlink Consultants said in a 1999 study of the proposed plant that the Burrup Peninsula location offers only a small freight advantage over the Middle East suppliers for Asian markets — about the same value as the penalty of higher gas prices incurred in Australia.

“The net delivered cost to Asian countries is about the same as from the Middle East assuming similar construction and manning costs,” the report said.

The problem that killed Agrium's plans for an Australian plant was that construction cost estimates were too high.

Agrium took a 51 percent equity participation in May 2002 in the Dampier Nitrogen Consortium, along with Plenty River Corp. Ltd. for 39 percent and Thiess Pty Ltd., with 10 percent. Agrium said in a 2003 presentation to the Resource Development Council in Anchorage that it was attracted to Western Australia because of a sizeable, competitively priced, natural gas supply; a positive political, business, and economic environment; synergies with the company's existing Pacific Rim production and marketing investments; and a growing domestic urea market.

The project development agreement expired in July 2003. Agrium announced in October 2003 that it was proceeding alone on the project because the parties could not resolve concerns over construction costs.

The company was subsequently unable to pare the construction cost to acceptable levels, and it has abandoned plans for an Australia plant for now, Gillespie told Petroleum News.

Burrup plant to open

A competing plant on the Burrup Peninsula has gone forward. That plant has a capacity to produce 760,000 metric tonnes per year of ammonia and is slated to start production in the second half of 2005, its owners said.

Norway's Yara International ASA said March 29 it would pay \$100 million to Burrup Holdings Pty. Ltd. for a 30 percent stake in the plant. According to its web site, Burrup Fertilisers Pty. Ltd. is a private company promoted by Oswal Projects Ltd. of New Delhi, India. The company was formed in Australia in 2000.

Yara had a previous agreement to market the plant's output. The company said the purchase strengthens its position in Asia and Oceania.

"With Burrup we have found an excellent strategic fit, including sound economics based on a competitive natural gas price and future development opportunities," said Yara President and chief executive Thorleif Enger.

At this point, the companies are considering construction of a second plant.

Development of the project was encouraged by the Western Australian government's A\$134 million multiuse infrastructure package, to upgrade the port, establish multi-user infrastructure corridors, establish and realign roads, and install inlet and outlet pipes for water desalination. An additional A\$20 million

was earmarked for a seawater desalination plant to support the project.

Population drives demand

It is not surprising that India's Oswal Projects is interested in Australian production of nitrogen. India nitrogen imports rose 12.3 percent in the 2001-2002 season, according to a world fertilizer study by the Food and Agriculture Association of the United Nations.

Worldwide, demand is projected to increase by 1.2 percent annually until 2008, the association said, adding that in terms of tonnage increases, Asia and Latin America will be the primary drivers of the growth.

The association said population growth would spur more fertilizer usage.

"Most high-quality agricultural land is already in production," the association said. "The marginal benefit of converting new land emphasizes the importance of continuing to improve crop yields so that existing agricultural lands can produce more food."

As available land and water resources decline in many developing countries, further growth in food production will depend on intensification of agriculture, the association said.

The association said 73 percent of the growth in nitrogen usage from 2003 to 2008 would occur in Asia, while 12 percent of the growth will be in Latin America.

Agrium is well positioned to benefit from Latin America market growth. The company has a 50 percent interest in a plant in Bahia Blanca, Argentina. It is the largest single train urea plant in the world and is capable of producing 1.1 million tonnes of urea annually. The plant has access to the Atlantic Ocean via a private tidewater terminal that provides access to export markets in South America and

around the world.

Agrium has added to its margins in Argentina by investing in a chain of retail outlets that feature its fertilizer products.

In North America, Agrium enjoys a gas cost advantage because of low gas prices at its plants in Alberta. Agrium stands to benefit from a recent industry trend of closing North American plants that have become uneconomic because of high gas prices.

Agrium hasn't given up on Alaska; its long-term plans for Alaska are focused on a much larger pool of gas than the Cook Inlet supply. The company has repeatedly said its Kenai facility is not for sale.

"We hope to relocate at some point in the future," said Lisa Parker, spokeswoman for the Kenai facility. "If North Slope gas becomes available and if there is a line that comes to Southcentral Alaska, Agrium would be interested."

According to Gillespie, the company is looking for overseas opportunities, but not in Australia. She said the company is taking a look at Trinidad as a plant location because of the country's ample supply of inexpensive gas.

Worldwide, Agrium builds where gas is trapped, Gillespie said. By following that strategy, the company takes some of the uncertainty out of the natural-gas-supply side of its equation.

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